



Taxation Reform for Small Businesses

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Taxation Reform for Small Businesses

Much has been written about the need for taxation reform in Australia which is a country with a high number of taxes e.g. best estimates show there are 99 at Federal level, 25 at State level and one at local government level. ([Tax Institute JOTHAM LIAN - 13 August 2018](#)).

That in itself indicates the complexity that has grown over years of Governments tinkering with taxes in order to raise revenues. There are several studies that show taxation can be an inhibitor of growth especially for small businesses. In many cases the Red Tape around the reporting and collection of taxes is also considered both cumbersome and costly.

1. Inhibiting Taxes

Polls in 2018 showed that the two most hated taxes are FBT and Payroll tax, both being seen as inhibitors to growth. Both these taxes raise large amounts of revenue nationwide:

- According to ABS data Payroll Tax raised around \$22.7 billion or about 28% of total taxation revenue for the Australian States
- The Institute of Public Accountants (IPA) which represents small businesses in Australia, said its members “go to extraordinary lengths” to avoid Payroll Tax. “They just don’t want to incur a tax they perceive as unfair,”
- IPA’s senior tax adviser Tony Greco told Accountants Daily “We’ve heard it directly from small businesses that some will just be happy not to grow so they stay underneath the threshold”.
- In a recent ‘My Business’ straw poll 24.6% of the 239 respondents ranked **Payroll Tax** as their most cumbersome tax in business, making it the third most disliked tax behind **GST** and **FBT**
- SMEs have hit back at Treasury claims that Payroll Tax has minimal impact on businesses, suggesting the “extremely unfair” tax is not just affecting business growth but also employee wages. ([Reporter ADAM ZUCHETTI - Tuesday, 17 April 2018](#))

2. Complexity

Taxation is now so complex that many small business owners find it difficult to understand the extent of their obligations including concessions and allowances. They default to their Accounting Advisers and pay the fees to have their tax situation sorted out.

Not so for Corporations, some of which can afford to use taxation specialists and may engage in-house taxation experts. Smaller employing organisations must be aware of their tax obligations at all times and depending upon category (size), small business can be responsible for:

- Superannuation (frequently lagging payments)
- PAYG withholding tax
- Payroll Tax depending on the threshold limit per State
- FBT calculations based on too many items e.g. vehicles/parking/loans & private expenses
- Owners annual tax rate on salary and/or other take-outs is too high in early years
- GST reporting & payment has high cost of compliance

Small business owners can be constantly under pressure to pay creditors, suppliers plus the need to pay staff *first* and the essential operating costs, causing owners to hold back available cash. The result can be to fall behind with taxation obligations which in the worst cases can lead to trading whilst insolvent and the embarrassment and damages in winding up.

3. Survival Rates

Small businesses generally require all the help they can get in their early years. Regardless of the reasons, the 'danger' years lie in the first 5 years. ABS records show that overall some 54% are still in business 5 years after commencing; therefore the dropout rate is around of half. Cash flow shortages are a major cause of failure when revenues are low and the costs of operation are rising, leading to the avoidance of taxation responsibilities.

ABS statistics: At the end of 2016-17 there were 2,238,299 actively trading businesses in the market sector in Australia, an increase of 3.1% from the end of 2015-16.

During this period the number of businesses **entering** the market was 328,205 being an increase of 5.7% or 17,770 units from 2015-16. The number of businesses **exiting** the market in 2016-17 was 261,450 being an increase of 0.5% (1,324) from 2015-16.

The gain between start-ups entering and small businesses leaving was 66,755 (20%).

The largest growth sector was in the un-employing small business sector; the very sector needing the most assistance...

Whilst there are a number of reasons why small businesses exit the market, results of this low net gain are alarming. When considered against the destruction caused to stakeholders, the lost opportunities for job engagement and the failure to establish financial independence for owners, it is economic vandalism not to act to improve such poor results.

4. Need for supporting policies

Australia now ranks 14th on the current World Bank scale of over 100 economies for 'Ease in Doing Business' having ranked 15th for some years. However some of the Countries rated are second and third world economies - Australia can do much better as a first world economy with some serious forethought and planning. A robust and growing small business sector is the backbone to many a contemporary economy due to the monetary circulation at the domestic base where spending fosters growth and sustainability. The world's current top 10 easiest economies in which to start a small business are listed below:

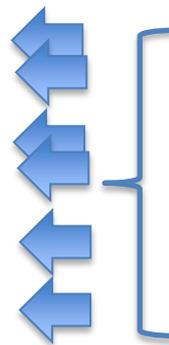
The ratings for being easiest consist of:

1. Registering a business
2. Tax breaks for small businesses
3. Electricity supply
4. Registering property
5. Obtaining credit
6. Protection for minority investors
7. Obtaining construction permits
8. Paying taxes

Base tax rates

1. New Zealand - Tax rate is 10% to 33%
2. Singapore - Tax rate is zero to 16.1%
3. Denmark - Tax rate is 22%
4. Korea - Tax rate is 10% to 25%
5. Hong Kong - Tax rate is 8.5% to 16%
6. United States- Tax rate is 21% max rate
7. United Kingdom - Tax rate is 9% average
8. Norway - Tax rate is 23% average
9. Georgia - Tax rate is 0% to 39.6%
10. Sweden - Tax rate is 22% top rate

14. Australia - Tax rate is 27.5%- one rate for all



Countries with early low tax rates to incentivize small business start-ups

1. New Zealand

Starting a business only takes a few hours thanks to simplified procedures. It is the best country when it comes to protecting minority investors as well as the best for starting a business. Its free trade agreements, pro-competition regulations, efficient tax codes and an open political system are all contributors to its ranking

2. Singapore

Continues to be the economy with the most business-friendly and secure environment. Resolving commercial disputes in Singapore's court system on average takes around 150 days; the shortest time in the world. In the U.S it takes 420 days and the cost is more than 31% of the claim.

3. Denmark

An effective **digitization process** is one of the prime factors contributing to its rank. Digitization allows quick and easy registration of new businesses, the acquisition of a 'NemID' signature and employee insurance registration. The procedures can be done in one day; the fee for starting a company costs 670 Kroner (\$98 USD)

(NemID is a log-in solution for Danish Internet banks, government websites and some private companies)

4. Korea

South Korea ranks towards the top due to strong results in obtaining electricity, trading across borders and enforcing contracts. This is supported by South Korea's super speedy **internet connection i.e. the fastest in the world**. The government has touted this fact in their initiatives since 2012 to attract entrepreneurs

5. Hong Kong

Starting a business is becoming more difficult in Hong Kong because of increased registration fees but there is a great deal of protection for minority investors. Partly because of this Hong Kong ranked high in terms of ease of starting a business, the simplicity of obtaining construction permits and conducting trade across the border.

6. United States

U.S corporate tax rates have been relatively steep but the country is able to make up by lowering costs for supplies, offices and logistics plus other. Despite ranking sixth it lags behind other developed countries when it comes to having an attractive business environment (which now appears to be changing).

7. United Kingdom

Up from eighth place in previous rankings. The World Bank reports it's the low costs associated with setting up a business, combined with increased levels of entrepreneurial optimism which contribute to the high ranking. Start-up costs are £81 (\$121.50 US) which is the low end in comparison to global norms.

8. Norway

Norway has managed to combine a strong technology sector and energetic workforce with a strong safety net of social programs. It has one of the most efficient systems on the globe to handle insolvency filings. The start-up procedure in Norway usually takes only four days and the relative cost to launch a venture is only 0.90% of annual per capita income.

9. Georgia This country is one of the world's top places to start a business. For years the middle-income country has been benefiting from an emerging economy. One of the reasons behind this is it only takes two days to register a business in Georgia and it only costs around the equivalent of \$40 US dollars.

10. Sweden High standards of living combined with one of the world's most skilled labour forces are among the many factors that Sweden is an excellent country within which to carry out commerce. Its strong infrastructure and well-developed social programs are supporting incentives as well.

These countries take steps to make it easy to start a business but also support and protect small investors. Costs are usually low, registrations are efficient and there are few red tape restrictions to slow early progress. Australia could do the same by overhauling its regulations, red tape, costs and fines and replace them with incentives that sustain small businesses and attract higher participation rates from willing entrepreneurs. We need to make it easier for small business to succeed!

5. Broad based taxes

Some countries have higher Sales / VAT taxes (similar to our GST) which range between 10% on the low side to 25% on the high side allowing them to mitigate or eliminate lower level taxes, thus relieving much of the associated red tape and related costs to Industry.

Broad based taxes are more efficient and less complex than targeted taxes. Raising the GST by 5% in Australia would generate some \$65bn (2018-2019) and may allow for the elimination of inefficient taxes and lower rates for others.

A patent already exist for the automation of the collection of GST and this should be seriously considered for adoption by Government. It has been estimated that small businesses spend on average \$2500 in fees to Accountants to assist with GST compliance. Therefore the estimated cost of GST compliance when spread cross the 2m or so small businesses is \$13bn which is a material saving to the sector. Automation would also lead to the permanent elimination of the GST unpaid backlog and completely obviate the need for BAS statements.

6. Conclusions

Australia needs to realise that the more complex tax applications become, the more they are exposed to manipulation and fraud. The higher the rates the more tax avoidance is adopted. Allowing small businesses to flourish in the formative years provides a larger tax take and increases employment as they mature. Tax incentives can be conducive to survival and attract more activity in establishing and growing small entities in the first place.

Some examples for Australia could be:

- 0 -10% tax over the first 3 years
- 11% - 15% over the next two years (to year 5) – then step up to max 20% for small enterprises with revenues under \$2.5m
- Low establishment fees in year one e.g. naming and registration fees at \$100. Eliminate Annual Return requirements and fees for first 3years.
- Personal tax for small business owners to be 10% for first 3 years; 15% for next two years for revenues under \$2.5m.
- FBT to be simplified and less expensive – this to stimulate business spending
- GST to be increased and automated to eliminate Industry costs, traded off against BAS reporting and reductions or eliminations of less effective taxes
- Payroll tax thresholds to be unified for all States; common thresholds to be lifted to \$2.5m

- Protections for owners to prevent bankruptcy by third parties during the first 3 years

We should not forget that big businesses started small. Destroying business whilst in their early stages can be tantamount to killing off a better future. Helping some and not others does not blunt the natural growth of a worthy business either i.e. one for which there is a demand. In Australia there is basically no protection for owners or minority shareholders and this is something that could be examined in other jurisdictions to measure the degree of successful outcomes.

In regions where business growth would assist local economies and generate employment it could be wise to extend incentives that encourage participation from enterprising small business owners. Such growth in itself could also generate secondary population growth because of access to products and services not previously or easily available.

With the population presently rising quite quickly in Australia it may be an opportune time to re-examine out attitude towards small business and its contribution to the national good.
